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October 21, 2016

Via Electronic Filing
Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: ***Ex Parte Communication*** *– Business Data Services in an Internet Protocol Environment*, WC Docket No. 16-143; *Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans*, WC Docket No. 15-247; *Special Access for Price Cap Local Exchange Carriers*, WC Docket No. 05-25; *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593

Dear Ms. Dortch:

On October 19, 2016, Chris Frentrup, Pete Sywenki, James Appleby, and the undersigned of Sprint Corporation ("Sprint"), along with Richard Metzger and Emily Daniels of Lawler, Metzger, Keeney & Logan, LLC, met with Pamela Arluk, Justin Faulb, William Kehoe, Christopher Koves, Richard Kwiatkowski, Eric Ralph, Deena Shetler, and Shane Taylor of the Wireline Competition Bureau. During the meeting, Sprint provided additional support for one aspect of Chairman Wheeler's proposal to reform the business data services ("BDS") marketplace – the "update of legacy TDM rules governing incumbent telephone companies [("LECs")] designed to address the artificially high prices being charged."[1] The record is replete with evidence that such action is overdue and represents a positive initial step toward repairing the broken BDS marketplace. Accordingly, Sprint urged the Commission to implement the proposed reforms as quickly as administratively practicable.

Furthermore, in support of the Chairman's framework, and to ensure the reforms accomplish their intended goals, Sprint proposed the following augmentations to the Chairman's proposal. In particular, Sprint focused on the proposal seeking to revise the current price cap regime to "account for over a decade of efficiency gains through a one-time downward

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[1] Fact Sheet, *Chairman Wheeler's Proposal to Promote Fairness, Competition, and Investment in the Business Data Services Market*, at 1-2 (rel. Oct. 7, 2016), http://transition.fcc.gov/Daily_Releases/Daily_Business/2016/db1007/DOC-341659A1.pdf ("Wheeler Fact Sheet").

adjustment of 11%" to the price cap index ("PCI"), as well as to "reduc[e] price caps going forward by an annual X factor reduction of 3%, offset by inflation."[2]

1. Implement the PCI Adjustment in Two Steps

In their agreement, Verizon and INCOMPAS urged the Commission to apply the "one-time rate adjustment in two steps."[3] There is no basis for deviating from this proposal and extending the adjustment period to three years as Chairman Wheeler proposes. Instead, the fact that "two of the entities who were once diametrically opposed have joined together" to urge the agency to act over a two-year period indicates that a two-year transition would not prove unduly burdensome for larger incumbent LECs.[4] Accordingly, if the Commission adopts an 11 percent adjustment, the PCI should be adjusted downward by just over 7 percent in the first year and just over 4 percent in the second year,[5] which would be in keeping with the Verizon/INCOMPAS agreement to apply the larger reduction in year one.[6]

To the extent there are concerns regarding the impact of a shorter transition on smaller price cap carriers, the appropriate response would be to provide smaller carriers with a three-year transition period (while maintaining the proposed two-year adjustment period for all other carriers). Extending the adjustment period to three years for all carriers would needlessly stall the benefits of reform, ultimately slowing the TDM-to-IP transition, dampening investment, and undermining competition.

2. Ensure that the PCI Adjustment Is Calculated Correctly

The Commission must ensure that the one-time adjustment corrects for the full understatement in the price cap indices that has occurred since the CALLS plan was completed in 2005. As noted, the Chairman's proposal would downwardly adjust the price caps by 11 percent to accomplish this.[7] By spreading the proposed 11 percent reduction over multiple

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[2] *Id*. at 1.

[3] Letter from Kathleen Grillo, Verizon, and Chip Pickering, INCOMPAS, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, at 1 (filed Aug. 9, 2016) ("Verizon/INCOMPAS Agreement").

[4] *See*, *e.g.*, *Business Data Services in an Internet Protocol Environment, Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans, Special Access for Price Cap Local Exchange Carriers, AT&T Corporation Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, Tariff Investigation Order and Further Notice of Proposed Rulemaking, 31 FCC Rcd 4723, ¶ 159 (2016) ("FNPRM" or "*Tariff Investigation Order*").

[5] *See* discussion *infra*.

[6] Verizon/INCOMPAS Agreement at 1.

[7] Wheeler Fact Sheet at 1.

years, however, the result will not be a full 11 percent reduction in the PCI. For example, define the current PCI to be 100. If the 11 percent reduction were taken immediately, the PCI would be reduced to 89. If the Commission adopts Sprint's proposed two-year adjustment of 7 percent in the first year and 4 percent in the second year, the PCI would be reduced to only 89.28 (= 100 * 0.93 * 0.96). Similarly, if the Commission adopted its proposed reductions of 3 percent in year one, 4 percent in year two, and 4 percent in year three, the PCI would be reduced to 89.3952 (= 100 * 0.97 * 0.96 * 0.96).

To ensure that the full 11 percent reduction is reflected after a multi-year transition, the Commission must adjust the reduction amounts taken in each year of the transition. Assuming a two-year adjustment period, the result would be a reduction of 7.14825 percent in year one and 4.14825 percent in year two. Likewise, if the Commission adopted its proposed three-year transition, the adjustments for each of the three years would be 3.14215 percent in year one, and 4.14215 percent in each of years two and three.

3. Ensure that the Incumbent LECs Cannot Unjustly Manipulate the Price Cap System

The Commission also must ensure that its actions "result in actual price reductions from current levels (i.e., not merely 'paper gains')."[8] To do so, the Commission cannot permit the incumbent LECs to manipulate the proposed reductions in a way that minimizes the resulting rate decreases or unduly discriminates against, or in favor of, particular customer groups. For example, absent appropriate constraints, the incumbents could target rate reductions to those services that are used by their wireless and enterprise affiliates while increasing the rates for services used by wireless and enterprise competitors.

Similarly, the incumbent LECs could target rate reductions to those services with declining demand and then increase the rates for BDS offerings with stable or growing demand. Assume, for example, that BDS Product A and BDS Product B have 100 units in base period demand and an initial price of $1,000 per unit. Further assume that demand for Product A is forecasted to decrease to 50 units, while demand for Product B is forecasted to remain at 100 units. Absent any reductions, future revenues would be $150,000. Following a 4 percent reduction, one would assume that future revenues would be $144,000. As shown below, however, the incumbent LEC functionally could avoid *one third* of this anticipated $6,000 decrease by applying all reductions to Product A – *i.e.*, the offering with declining demand.

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8 Verizon/INCOMPAS Agreement at 23.

		Forecasted Demand	Proposed Price	Realized Future Revenues
Apply Decreases Proportionately	Product A	50	$960	$48,000
	Product B	100	$960	$96,000
				= $144,000
Apply Decreases to Product with Declining Demand	Product A	50	$920	$46,000
	Product B	100	$1,000	$100,000
				= $146,000

The incumbents also could target rate reductions to services that lock customers into long-term plans while increasing the rates for shorter-term offerings. Many carriers require flexibility to undertake the TDM-to-IP transition efficiently and successfully. Absent effective constraints, the incumbents would be able to force purchasers to choose either to (1) forego that much-needed flexibility by committing to a longer term or (2) pay an excessive penalty. Either choice benefits the incumbents while undermining the Commission's goals and harming purchasers (and, ultimately, consumers).

For example, Sprint's calculations for AT&T's BellSouth DS1 Zone 1 show that AT&T could *double* the average circuit price for all plans that are not based on long-term volume commitments and still readily accomplish either an 8 percent overall reduction (*i.e.*, assuming a 7 percent reduction for year one and a further 1 percent reduction for the X-factor offset by inflation) or a 4 percent overall reduction (*i.e.*, assuming the proposed 3 percent reduction for year one and a further 1 percent reduction for the X-factor offset by inflation).

Accomplishing an 8 Percent Reduction			
Service Plan	**Approx. Percentage of Current Revenues**	**Potential Action**	**Resulting Percentage of Current Revenues**
Month-to-Month	12.25%	Double Rate	24.50%
24-48 Months	1.63%	Double Rate	3.26%
24-48 Months – Volume Plan	30.64%	Reduce Rate by 32.3%	20.74%
49-72 Months	4.49%	Double Rate	8.98%
49-72 Months – Volume Plan	50.99%	Reduce Rate by 32.3%	34.52%
			= 92%

Accomplishing a 4 Percent Reduction			
Service Plan	**Approx. Percentage of Current Revenues**	**Potential Action**	**Resulting Percentage of Current Revenues**
Month-to-Month	12.25%	Double Rate	24.50%
24-48 Months	1.63%	Double Rate	3.26%
24-48 Months – Volume Plan	30.64%	Reduce Rate by 27.4%	22.24%
49-72 Months	4.49%	Double Rate	8.98%
49-72 Months – Volume Plan	50.99%	Reduce Rate by 27.4%	37.02%
			= 96%

The Commission already has concluded that the incumbent LECs have abused the flexibility they have been granted in the BDS marketplace thus far.[9] Moreover, the incumbent LECs have proven that they have both the incentive and ability to undermine the Commission's intended reforms going forward. In response to the *Tariff Investigation Order*, both AT&T and Verizon announced actual or effective price increases across all geographic areas for the services in question. Verizon offset required reductions in commitment shortfall penalties with an increase in channel termination rates.[10] AT&T removed circuit portability from its service plan offerings to offset the removal of all-or-nothing provisions, excessive shortfall penalties, and early termination liabilities from its service plans.[11] These tactics signal the incumbents' willingness to undermine even the limited BDS reform efforts that have been proposed.

Simply stated, the Commission must implement a safeguard to prevent unreasonable pricing manipulations. Only by doing so can the Commission ensure that its reforms result in real-world cost reductions equitable to all customer classes and that its reforms fulfill the agency's overarching BDS goals of "ensur[ing] rates, terms and conditions are at just and reasonable levels," "facilitating technology transitions," "promoting competition," "protecting customers," and "learn[ing] from past experiences."[12] In particular, Sprint proposes adoption of the rule reflected in the attachment hereto.

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9 *See*, *e.g.*, *Tariff Investigation Order* ¶ 87 (declaring certain terms and conditions implemented by the incumbent LECs to be "unreasonable practices under section 201(b)").

10 *See* Verizon Telephone Companies, Tariff F.C.C. Nos. 1, 11, 14 and 16, Transmittal No. 1335, Description and Justification, at 4 (July 1, 2016).

11 *See* Ameritech Operating Companies Tariff F.C.C. No. 2, Transmittal No. 1847, Description and Justification (July 1, 2016); Pacific Bell Telephone Company Tariff F.C.C. No. 1, Transmittal No. 539, Description and Justification (July 1, 2016); Southwestern Bell Telephone Company Tariff F.C.C. No. 73, Transmittal No. 3428, Description and Justification (July 1, 2016).

12 *See*, *e.g.*, FNPRM ¶¶ 290, 291, 292, 423, 492.

Pursuant to this rule, the Commission would require each incumbent LEC subject to the updated price cap regime to reduce its special access basket PCI to reflect the one-time reduction and annual X-factor, offset by inflation. For example, if the special access PCI is reduced by 7 percent in year one and the X-factor less inflation is 1 percent, then the PCI for the special access basket must be reduced by 8 percent. To implement this overall reduction to the special access basket, each carrier would have to demonstrate that the pricing for each service plan category offering (*i.e.*, month-to-month, term, term with volume commitment) within each DS1 and DS3 zone was reduced by the same percentage as the overall special access basket PCI reduction.[13] Because the special access basket's API is a weighted average of each of these service plan categories, an 8 percent reduction in each of the categories would result in an 8 percent reduction in the basket as well.

This interim safeguard would merely maintain the existing pricing relationships among the various BDS categories and subcategories, and thus ensure fairness to all purchasers while imposing no undue harm to incumbent LECs.[14] Moreover, once the one-time adjustment is fully implemented, the incumbents would be required only to apply the annual adjustment to the BDS PCI and would retain the flexibility to adjust rates accorded carriers under the current Part 61 rules.[15]

The Commission has ample authority to implement this proposal, which plainly is designed to ensure that rates are just, reasonable, and non-discriminatory pursuant to sections 201(b) and 202(a) of the Communications Act of 1934, as amended (the "Act").[16] Courts accord substantial deference to the Commission's interpretation of the terms "just" and "reasonable" in section 201(b) and "unjust" and "unreasonable" in section 202(a).[17] Importantly, courts have

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[13] Because each service plan category offering would have several rate elements, including channel terminations and fixed and per-mile transport costs, the incumbent LECs would continue to have their existing flexibility to vary individual rates within the offerings, subject to this overall limitation.

[14] At the very least, should the Commission eschew this proposal, it should adopt a flat prohibition on increasing rate elements and clarify that the reductions it adopted should not result in rate increases for any customer. *See* Letter from Paul Margie, Counsel for Sprint Corporation, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, Attachment at 7 (filed. Oct. 14, 2016).

[15] 47 C.F.R. §§ 61.41 *et seq.*

[16] *See* 47 U.S.C. §§ 201(b), 202(a).

[17] *See Capital Network Sys., Inc. v. FCC*, 28 F.3d 201, 204 (D.C. Cir. 1994) ("Because 'just,' 'unjust,' 'reasonable,' and 'unreasonable' are ambiguous statutory terms, this court owes substantial deference to the interpretation the Commission accords them."); *Orloff v. FCC*, 352 F.3d 415, 420 (D.C. Cir. 2003) (discussing how "the 'generality of these terms' – unjust, unreasonable – 'opens a rather large area for the free play of agency discretion, limited of course by the familiar 'arbitrary' and 'capricious' standard") (quoting *Bell Atl. Tel. Cos. v. FCC*, 79

been "'particularly deferential' when reviewing Commission ratemaking decisions '[b]ecause agency ratemaking is far from an exact science and involves 'policy determinations in which the agency is acknowledged to have expertise.'"[18]

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For the reasons outlined above, the Commission should ensure that the correction to the current PCIs results in the full 11 percent adjustment contemplated in Chairman Wheeler's proposal. The Commission also should adopt safeguards to ensure that the price reductions associated with the one-time price cap adjustment are shared equitably. By taking these limited actions, the Commission will better "enhance competitive LECs' ability to respond to the changing nature of the business data services market, minimize disruption of incumbent LEC's tariffs, and accelerate the adoption of IP technologies to the benefit of consumers."[19] Conversely, implementing the proposed BDS regime without measures that guard against the incumbent LECs' predictable schemes would undermine BDS reform before it can even begin in earnest, ensuring that the BDS marketplace will continue to be broken for all services.

F.3d 1195, 1202 (D.C. Cir. 1996)); *see also* Letter from Thomas Jones, Counsel for Birch Communications, Inc., BT Americas Inc., and Level 3 Communications, LLC, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 05-25, at 1-2 (filed Aug. 28, 2015) ("Joint CLEC *Ex Parte*").

[18] Joint CLEC *Ex Parte* at 2 (quoting *Time Warner Entm't Co., L.P. v. FCC*, 56 F.3d 151, 164 (D.C. Cir. 1995) (internal citation omitted)). The proposals set forth herein also do not involve the setting of individual rates and thus do not require a rate prescription proceeding pursuant to section 205 of the Act. As the Joint CLECs have noted, the "application of price caps does not constitute an actual or *de facto* rate prescription." Joint CLEC *Ex Parte* at 4. *See also id*. at 5; AT&T, Brief of Petitioners, *In Re AT&T Corp.*, No. 03-1397, at 42 (D.C. Cir. Aug. 20, 2004) ("It is well-settled that the imposition of price caps is not a rate prescription, but only a 'safe harbor' of rates that are presumptively lawful.").

[19] *Tariff Investigation Order* ¶ 87.

Pursuant to section 1.1206 of the Commission's Rules, a copy of this letter is being filed electronically in the above-referenced dockets. If you have any questions, please feel free to contact me at (703) 433-3786.

Respectfully submitted,

/s/ Charles W. McKee

Charles W. McKee
Vice President, Government Affairs
Federal & State Regulatory

cc: Meeting participants

Attachment

Attachment A

Proposed Rule[20]

Section 61.__ Implementation of the PCI Adjustment: 2017 and 2018 Annual Filings

(a) For the 2017 annual filing, each price cap local exchange carrier shall:

(1) Adjust the PCI for the special access basket specified in § 61.42(d)(5) downward by the sum of:

(i) The adjustment required by § 61.45(b)(1); and

(ii) A minimum of 7.14825 percent.

(2) For DS1 and DS3 services:

(i) Calculate the revenues for each month-to-month, term, and term with volume commitments offering within each DS1 and DS3 pricing zone using demand from the most recent calendar year; and

(ii) Reduce the resulting revenue amounts by the same total percentage calculated in paragraph (a)(1) of this section.

(b) For the 2018 annual filing, each price cap local exchange carrier shall make the same adjustments set forth in paragraphs (a)(1) and (2) of this section, except that the reduction in paragraph (a)(1)(ii) must be a minimum of 4.14825 percent.

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20 For purposes of the draft rule, Sprint assumes that the one-time reduction is intended to result in an 11 percent reduction to the current PCI and is carried out over a two-year period. If the overall adjustment or the adjustment period ultimately adopted were different, the proposed rule could be modified easily. In doing so and as noted *supra* at 2-3, the Commission should ensure that its overall PCI reduction is fully realized.